

VZCZCXYZ0025
PP RUEHWEB

DE RUEHPE #0785/01 0751517
ZNR UUUUU ZZH
P 161517Z MAR 07
FM AMEMBASSY LIMA
TO RUEATRS/DEPT OF TREASURY WASH DC PRIORITY
RUEHC/SECSTATE WASHDC PRIORITY 4415
INFO RUEHAC/AMEMBASSY ASUNCION PRIORITY 1624
RUEHBO/AMEMBASSY BOGOTA PRIORITY 4456
RUEHBR/AMEMBASSY BRASILIA PRIORITY 7250
RUEHBU/AMEMBASSY BUENOS AIRES PRIORITY 2823
RUEHCV/AMEMBASSY CARACAS PRIORITY 0217
RUEHGT/AMEMBASSY GUATEMALA PRIORITY 1002
RUEHLP/AMEMBASSY LA PAZ MAR 4112
RUEHME/AMEMBASSY MEXICO PRIORITY 3478
RUEHMN/AMEMBASSY MONTEVIDEO PRIORITY 9129
RUEHQT/AMEMBASSY QUITO PRIORITY 1086
RUEHSG/AMEMBASSY SANTIAGO PRIORITY 1173
RHEHAAA/NATIONAL SECURITY COUNCIL WASHINGTON DC PRIORITY
RUMIAAA/USCINCSO MIAMI FL PRIORITY

UNCLAS LIMA 000785

SIPDIS

SENSITIVE
SIPDIS

E.O. 12958: N/A
TAGS: [PGOV](#) [PREL](#) [ECON](#) [ETRD](#) [EFIN](#) [ENRG](#) [PE](#)
SUBJECT: SCENE SETTER FOR SECRETARY PAULSON

¶1. (SBU) Secretary Paulson: Welcome to Peru. Your visit provides an excellent opportunity to affirm USG support for the Garcia government's efforts to reduce poverty and expand social inclusion through continued market-oriented, investment-friendly growth policies.

¶2. (SBU) Peruvian government officials, including President Garcia and Foreign Minister Garcia Belaunde, were initially disappointed that President Bush's trip to Latin America did not include Peru. This feeling was assuaged by the announcement that the President would travel to Lima for APEC 2008, by a presidential phone call in late February, and by your visit. President Garcia has welcomed the policy-level attention from Washington, and is particularly pleased with your visit. In past meetings, he has underscored his commitment to democratic government and an open economy, and reiterated his conviction that the relative success of this pragmatic political-economic model in improving the lives of all people, especially the poor, will be pivotal in defeating the statist, autocratic alternative embodied in Venezuelan President Hugo Chavez' "Bolivarian" revolution. Integral to this effort, Garcia has said, is U.S. Congressional approval of the U.S.-Peru Free Trade Agreement, formally known as the Peru Trade Promotion Agreement (PTPA). You can expect a similar message during your meeting with him.

¶3. (SBU) In his first seven months in office, President Garcia has dispelled many doubts about whether he had learned needed lessons from his troubled first term (85-90) with respect to the economy. He has continued policies favoring macro-economic stability and security for investment that were implemented by his predecessor, while accelerating efforts to direct the benefits of growth to the provinces and the poor. This is understandable given the Peru's recent record: an average of 5% growth over the past six years, 7% growth in 2006 and a projected growth rate of 8% for this year. Fueled in part by high mineral prices, exports and per capita GDP figures have likewise registered significant increases over the past five years.

¶4. (SBU) Garcia has also resisted populist pressures on a number of sensitive economic questions. One early such question was a call to eliminate the basic service charge ("renta basica") for users of the national telephone company,

Telefonica. While the ruling APRA party had campaigned in favor, in power it eventually pursued a more pragmatic course that resulted in a negotiated agreement between the government and the company to reduce (but not eliminate) the basic service charge. Similarly, the government managed to deflect moves to "nationalize" the vital mining industry (a la Bolivia with its hydrocarbons industry) or to compel renegotiation of legally established contracts. Either of these approaches would have undermined investor confidence in Peru and interrupted the country's steady climb toward "investment grade" status -- an explicit government goal. Instead the government seized as its own a behind the scenes proposal from the private sector under which mining companies make "voluntary contributions," on a sliding scale of 1 to 3.75% of after tax profits (depending on the size of the company), to invest in infrastructure and social projects in the regions and communities in which they operate.

15. (SBU) If Peru's macro-economic numbers are excellent, persistent poverty remains the central political challenge. Close to half of Peruvians, mostly in the southern highlands and Amazonian lowlands, continue to live below the poverty line. Notwithstanding the economic growth, wealth has failed to "trickle down" in a politically satisfying way -- up to now. President Garcia, who beat his populist rival Ollantu Humala in the 2006 elections by a 5% margin, understands the urgency of this challenge. That is, he knows that if his government is to succeed and Peru is to consolidate its current positive transformation, economic growth and market-friendly policies must be used to reduce poverty and to bring in the mass of Peruvians as full beneficiaries of the country's supposed success.

16. (SBU) Garcia's social policy consists of two inter-related planks. The first is to consolidate Peru's tangle of social support programs from 80 down to 20, to reduce bureaucratic overhead costs and to ensure the government's limited funds get directly into the hands of those who most need them. The second plank is to significantly increase social spending, with a focus on education, clean water and electrification. In this connection, Garcia has no bones about borrowing and expanding ideas from his predecessor such as "Juntos" ("Together") -- a program that gives financial incentives for poor families to keep their children in school. As a first step toward education reform, the government has also moved to break the asphyxiating stranglehold on public schools of the Maoist national education union (Sutep).

17. (SBU) In addition, Garcia has inaugurated his own signature social programs: "Sierra Exportadora" ("Exporting Highlands"), which aims to fight poverty by linking small rural producers to national and international markets; "Agua Para Todos" ("Water for Everyone"), intended to make clean drinking water available to poor urban and rural communities; and accelerated decentralization, to transfer money and decision-making authority from the central government (where it remains highly concentrated) to the regions and municipalities. These programs remain more idea than reality at this point, and have faced a range of concrete obstacles in their implementation. For example, transfer of funds and spending authority from the central government to the regions has been slowed by concern that regional and municipal governments are ill prepared to take on these new responsibilities, by the central government's own administrative incapacity and by a series of ministerial spending scandals that some observers blame on the government's impatience to rush to work without having laid the necessary institutional groundwork first.

18. (SBU) You will note a clear convergence in the themes struck by President Bush during his Latin America visit -- the importance of democracy, investing in people, improving education and health, and free trade -- with the policy priorities of the Garcia administration. Your visit is a timely opportunity to underscore these convergences and to reiterate USG support for Garcia's economic management. I look forward to having you with us in Peru.

STRUBLE